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**UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF CALIFORNIA**

EFRAIN MUNOZ, LEONA LOVETTE,
STEPHANIE MELANI, individually and on
behalf of all others similarly situated,

Plaintiffs,

v.

PHH CORP., PHH MORTGAGE CORP.,
PHH HOME LOANS, LLC, ATRIUM
INSURANCE CORP.

Defendants.

CASE NO.: 1:08-CV-759 AWI-DLB

**FIRST AMENDED CLASS ACTION
COMPLAINT**

JURY TRIAL DEMANDED

1 Plaintiffs Efrain Munoz, Leona Lovette, Stephanie Melani, Iris Grant, John Hoffman and
2 Daniel Maga, II, (collectively "Plaintiffs"), on behalf of themselves and a class of all others similarly
3 situated, allege as follows:

4 **INTRODUCTION**

5 1. PHH Corporation, one of the nation's largest financial services companies, together
6 with certain participating subsidiaries and/or affiliates, including PHH Mortgage Corporation ("PHH
7 Mortgage") and PHH Home Loans, LLC ("PHH Home Loans"), operating under various trade names
8 (collectively referred to herein as "PHH" or the "Company") has acted in concert with its wholly-
9 owned reinsurer, Atrium Reinsurance Corporation ("Atrium"), previously known as Atrium Insurance
10 Corporation, to effectuate a scheme whereby, in violation of the Real Estate Settlement Procedures
11 Act of 1974 ("RESPA"): (a) illegal referral payments in the form of purported reinsurance premiums
12 are paid by private mortgage insurers to Atrium; and (b) through Atrium, PHH receives an unlawful
13 split of private mortgage insurance premiums paid by its borrowers.

14 2. This is a proposed national class action brought by Plaintiffs on behalf of themselves
15 and a class of all other similarly situated homeowners who obtained residential mortgage loans
16 through PHH or any of its subsidiaries and paid for private mortgage insurance issued by insurers with
17 whom PHH had captive reinsurance arrangements. In this action, Plaintiffs challenge a secretive
18 conspiracy to circumvent RESPA's prohibition against kickbacks and unearned fees. Members of the
19 conspiracy included PHH Corporation, PHH Home Loans, PHH Mortgage, Atrium and unnamed co-
20 conspirator private mortgage insurers.

21 3. Homeowners who buy a home with less than a 20% down payment are typically
22 required to pay for private mortgage insurance. Private mortgage insurance protects the lender in the
23 event of a default by the borrower. The premium is paid by the borrower and is usually collected by
24 the lender with the borrower's monthly payments. Borrowers typically have no opportunity to
25 comparison-shop or select the private mortgage insurer.

26 4. Section 2607 of RESPA prohibits lenders from: (a) accepting kickbacks or referral fees
27 from any person providing a real estate settlement service, including providers of private mortgage
28

1 insurance; and (b) accepting any portion of a settlement service fee—including amounts paid by
2 borrowers for private mortgage insurance—other than for services actually performed. Thus, a lender
3 cannot legally accept a kickback or any unearned portion of a premium from the insurer issuing the
4 private mortgage insurance policy on the borrower's home.

5 5. Nonetheless, in defiance of RESPA's unambiguous mandate, PHH attempted to
6 circumvent the statute's prohibition against accepting kickbacks and unearned fees by arranging for
7 private mortgage insurers to pay an excessive portion of borrowers' private mortgage insurance
8 premiums to Atrium in the form of purported reinsurance premiums.

9 6. While these payments to PHH's wholly-owned subsidiary were purportedly for
10 "reinsurance" services, Atrium received these payments while assuming no actual, little, or
11 incommensurate risk vis-à-vis the premium ceded to the reinsurer. For instance, during the period
12 beginning in the year 2000 through the end of 2007, PHH's captive reinsurer received over
13 \$327,000,000 from leading primary mortgage insurers as its "split" of borrowers' mortgage insurance
14 premiums—over \$32,000,000 in 2007 alone. In stark contrast, during such time period, its actual
15 insurance losses as reflected in the total amount of claims paid were zero. In other words, the
16 hundreds of millions of dollars collected by PHH through its captive reinsurance arrangements far
17 exceeded the value of any services rendered.

18 7. This scheme constitutes disguised, unlawful referral fees in violation of RESPA's anti-
19 kickback provisions, as well as a violation of RESPA's ban on accepting a percentage of settlement-
20 service fees other than for services actually performed.

21 **JURISDICTION AND VENUE**

22 8. This Court has subject matter jurisdiction over this action pursuant to 28 U.S.C. §§
23 1331 and 1367 and 12 U.S.C. § 2614.

24 9. Venue is proper in this district under 28 U.S.C. § 1391(b) and 12 U.S.C. § 2614
25 because the real property involved in one or more of Plaintiffs' mortgage loan transactions is located
26 in this district. Further, Defendants reside in this district and a substantial part of the events giving rise
27 to the claims occurred in this district.
28

PARTIES

Plaintiffs

10. Plaintiff Efrain Munoz resides in Shafter, CA. On or about June 2, 2007, Plaintiff Munoz obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment of less than 20%. Plaintiff Munoz was required to pay for private mortgage insurance from a provider with whom PHH had a captive reinsurance arrangement. Plaintiff Munoz was given no opportunity to select his private mortgage insurer; rather, the insurer was selected by PHH.

11. Plaintiff Leona Lovette resides in Sharon Hill, PA. On June 11, 2007, Plaintiff Lovette obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment of less than 20%. Plaintiff Lovette was required to pay for private mortgage insurance from a provider with whom PHH had a captive reinsurance arrangement. Plaintiff Lovette was given no opportunity to select her private mortgage insurer; rather, the insurer was selected by PHH.

12. Plaintiff Stephanie Melani resides in Erie, PA. On or about June 7, 2007, Plaintiff Melani obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment of less than 20%. Plaintiff Melani was required to pay for private mortgage insurance from a provider with whom PHH had a captive reinsurance arrangement. Plaintiff Melani was given no opportunity to select her private mortgage insurer; rather, the insurer was selected by PHH.

13. Plaintiff Iris Grant resides in Thousand Oaks, CA. On or about December 31, 2007, Plaintiff Grant obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment of less than 20%. Plaintiff Grant was required to pay for private mortgage insurance from a provider with whom PHH had a captive reinsurance arrangement. Plaintiff Grant was given no opportunity to select her private mortgage insurer; rather, the insurer was selected by PHH.

14. Plaintiff John C. Hoffman resides in Chicago, IL. On or about October 1, 2008, Plaintiff Hoffman obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment of less than 20%. Plaintiff Hoffman was required to pay for private mortgage insurance from a provider with whom PHH had a captive reinsurance arrangement. Plaintiff Hoffman was not given an opportunity to select his private mortgage insurer; rather, the insurer was selected by PHH.

1 15. Plaintiff Daniel M. Maga, II resides in Chicago, IL. On or about June 27, 2008, Plaintiff
2 Maga obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment
3 of less than 20%. Plaintiff Maga was required to pay for private mortgage insurance from a provider
4 with whom PHH had a captive reinsurance arrangement. Plaintiff Maga was not given an opportunity
5 to select his private mortgage insurer; rather, the insurer was selected by PHH.

6 **Defendants**

7 16. Defendant PHH Corporation is a Maryland corporation, with its corporate headquarters
8 located at 3000 Leadenhall Rd., Mt. Laurel, New Jersey. PHH does business in all fifty states.
9 Defendant PHH Corp., the parent company of the other Defendants in this case, is a proper party to this
10 action, as it: (a) participated in the unlawful scheme described herein; and (b) was and is a beneficiary
11 of the unlawful kickbacks and unearned fees described herein. *See, e.g., 2007 Form 10-K Submission*
12 *to the Securities and Exchange Commission, filed February 29, 2008 ("2007 10-K")* ("We also
13 generate revenue from reinsurance activities from our wholly owned subsidiary, Atrium Insurance
14 Corporation"). Further, upon information and belief, Atrium funnels reinsurance premiums to PHH
15 Corporation. At any rate, regardless of whether Atrium paid dividends to PHH Corporation, PHH
16 Corporation received substantial pecuniary benefit from its unlawfully-orchestrated captive reinsurance
17 arrangements. Under RESPA Section 8(b), 12 U.S.C. 2607(b), it is unlawful for any person to accept
18 any portion of an unearned fee. Section 8(d) of RESPA, 12 U.S.C. § 2607(d), provides that a violator is
19 jointly and severally liable for three times the amount paid for the settlement service.

20 17. Defendant PHH Mortgage is a New Jersey corporation and a subsidiary of Defendant
21 PHH Corporation. PHH Mortgage was formerly known as "Cendant Mortgage."

22 18. Defendant PHH Home Loans is a Delaware limited liability company and a subsidiary
23 of Defendants PHH Corporation and Defendant PHH Mortgage.

24 19. Defendant Atrium Insurance Corporation was a subsidiary of PHH and incorporated in
25 New York. On November 12, 2009, Atrium incorporated in the State of Vermont as Atrium
26 Reinsurance Corporation, and assumed all premiums and liabilities of Atrium Insurance Corporation.
27
28

FACTUAL ALLEGATIONS

PHH's Operations

20. PHH is one of the nation's largest originators of residential mortgage loans, as well as one of the country's biggest outsource providers of mortgage origination services. Prior to February 1, 2005, PHH was a subsidiary of Cendant Corp. (renamed Avis Budget Group, Inc.). Effective February 1, 2005, PHH was spun off as an independent, publicly traded company. See 2007 Form 10-K Submission to the Securities and Exchange Commission, filed February 29, 2008 ("2007 10-K").

21. The Company originates and services mortgage loans primarily through PHH Mortgage and its subsidiaries, one of which is PHH Home Loans. PHH Home Loans has also conducted business under various assumed names, including Sunbelt Lending Services, Hamera Home Loans, ERA Home Loans, Burnett Home Loans, Coldwell Banker Home Loans, Cartus Home Loans, First Capital and Coastal Funding. *See Id*; *See also* Exhibit 21 to 2007 10-K.

22. Through its subsidiary Atrium, PHH enters into agreements to provide purported reinsurance services to primary private mortgage insurance providers with respect to mortgage loans originated, funded and/or serviced by PHH.

23. Atrium, a monoline mortgage guaranty insurance company, receives premiums from certain third-party private mortgage insurance companies that insure loans originated by PHH's mortgage production division. *See* 2007 10-K.

Private Mortgage Insurance Industry

24. In order to lessen risk of default, lenders typically prefer to finance no more than eighty percent of the value of a home, with the remaining twenty percent being paid as a down payment by the borrower. In the event of a default, the lender is then more likely to completely recover its investment.

25. Many potential homebuyers cannot afford to pay 20% of the purchase price as a downpayment on a home. Private mortgage insurance allows the lender to make loans in excess of 80% of the home's value by providing a guarantee from a dependable third party—the private mortgage insurer—to protect the lender in the event of a default by the borrower.

1 26. Private mortgage insurers are typically unaffiliated third-party companies who agree to
2 cover the first twenty to thirty percent of the amount of the potential claim, including unpaid principal,
3 interest and certain expenses.

4 27. The amount of private mortgage insurance coverage required varies according to the
5 perceived risk of default. The lower the percentage of the borrower's down payment, the more
6 mortgage insurance required. For example, more private mortgage insurance is required with a five
7 percent down payment than with a fifteen percent down payment. Additionally, more private mortgage
8 insurance may be required for adjustable-rate mortgages than for fixed-rate mortgages.

9 28. While the lender is the beneficiary of the private mortgage insurance, the borrower pays
10 the premiums, usually through an addition to the borrower's monthly mortgage payment.

11 29. Borrowers generally have no opportunity to comparison-shop for private mortgage
12 insurance. The private mortgage insurer is selected by the lender. The terms and conditions of the
13 insurance policy, as well as the cost of the policy, is determined by the lender and the private mortgage
14 insurer, rather than negotiated between the borrower and the private mortgage insurer.

15 30. The private mortgage insurance industry began with the founding of Mortgage Guaranty
16 Insurance Corp. ("MGIC") in 1957 and is dominated by MGIC and other companies, including,
17 without limitation: PMI Mortgage Insurance Company, Genworth Mortgage Insurance Corporation,
18 Radian Guaranty Inc., AIG United Guaranty, Triad Guaranty Insurance Corporation and Republic
19 Mortgage Insurance Company. Generally, the industry is represented by a trade association known as
20 Mortgage Insurance Companies of America ("MICA"). According to its website, MICA's members
21 include each of the foregoing insurers, with the exception of Radian Guaranty.

22 31. According to MICA, new private mortgage insurance contracts for its member firms
23 have consistently exceeded \$200 billion per year since 1998. MICA member-firms issued over 1.4
24 billion new certificates of mortgage insurance in 2006, representing over \$226 billion in new insurance
25 written. MICA 2007-2008 Fact Book & Membership Directory, available at www.PrivateMi.com.

26 32. Private mortgage insurance is limited to the conventional home loan market. Mortgage
27 loans directly insured by the federal government via mortgage guaranty programs, such as those
28

maintained by the Federal Housing Administration and the Veterans Administration, maintain their own form of mortgage default insurance.

RESPA Prohibits Kickbacks for Referrals and Fee-Splitting Related To Private Mortgage Insurance Policies

33. RESPA is the primary federal law regulating residential mortgage settlement services. The United States Department of Housing and Urban Development (“HUD”) is charged with enforcing RESPA. HUD has promulgated the implementing rules for RESPA. See Regulation X, 24 C.F.R. § 3500.

34. RESPA was enacted, in part, to curb the problem of kickbacks between real estate agents, lenders and other real estate settlement service providers. “It is the purpose of this chapter to effect certain changes in the settlement process for residential real estate that will result...(2) in the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services.” 12 U.S.C. § 2601(b).

35. A key component of RESPA is its dual prohibition of referral fees and fee-splitting between persons involved in real estate settlement services.

36. In 12 U.S.C. 2607(a) RESPA provides:

No person shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person.

37. In 12 U.S.C. 2607(b) RESPA provides:

No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed.

38. Regulation X further explains, “A charge by a person for which no or nominal services are performed or for which duplicative fees are charged is an unearned fee and violates this section.” 24 C.F.R. § 3500.14(c).

1 39. The term “thing of value” is broadly defined in RESPA and further described in
2 Regulation X as including:

3 without limitation, monies, things, discounts, salaries, commissions,
4 fees, duplicate payments of a charge, stock, dividends, distributions of
5 partnership profits, franchise royalties, credits representing monies that
6 may be paid at a future date, the opportunity to participate in a money-
7 making program, retained or increased earnings, increased equity in a
8 parent or subsidiary entity...The term payment is used as synonymous
9 with the giving or receiving any “thing of value” and does not require
10 transfer of money.

11 24. C.F.R. § 3500.14(d).

12 40. Private mortgage insurance business referred to private mortgage insurers by a lender
13 constitutes “business incident to or a part of a real estate settlement service” within the meaning of
14 RESPA, 12 U.S.C. § 2607(a). The term “settlement service” is liberally defined in RESPA and
15 Regulation X and includes the “provision of services involving mortgage insurance.” 24 C.F.R. §
16 3500.2(b).

17 41. Under RESPA, therefore, a lender is prohibited from accepting referral fees from a
18 private mortgage insurer or from splitting private mortgage insurance premiums with the insurer other
19 than for services actually performed.

20 **Mortgage Reinsurance Industry**

21 42. Private mortgage insurers may enter into contracts with reinsurers, whereby the
22 reinsurer typically agrees to assume a portion of the private mortgage insurer’s risk with respect to a
23 given pool of loans. In return, the private mortgage insurer pays to the reinsurer a portion of the
24 premiums it receives from borrowers with respect to the loans involved.

25 43. Mortgage reinsurance arrangements can generally take two forms: (a) “quota share”
26 and (b) “excess of loss.”

27 44. In a quota share reinsurance arrangement, the reinsurer agrees to assume a fixed
28 percentage of all the private mortgage insurer’s insured losses. Thus, if the private mortgage insurer
experiences losses, the reinsurer is certain to experience losses in the percentage agreed upon in the
reinsurance coverage.

1 45. In an excess of loss reinsurance arrangement, however, the reinsurer is liable only for
2 claims, or a percentage thereof, above a particular level (the “entry point”). Unlike the quota share
3 arrangement, the excess of loss method does not necessarily result in any risk of loss being shifted to
4 the reinsurer, and, further, can unscrupulously be manipulated to, essentially, ensure that the reinsurer
5 will never incur actual losses.

6 46. The likelihood of the reinsurer experiencing any losses under this arrangement depends
7 not only on the amount of losses by the private mortgage insurance, but also on whether the
8 reinsurance agreement between the reinsurer and the private mortgage insurer sets the entry point for
9 the reinsurer at a level where the reinsurer bears actual risk of loss.

10
11 **Captive Mortgage Reinsurance Arrangements and HUD’s Concern About RESPA Anti-**
12 **kickback Violations Under Such Arrangements**

13 47. Private mortgage insurers collect billions of dollars in premiums from customers
14 produced by home mortgage lenders. Certain lenders, seeking to capitalize on the billions of dollars
15 their borrowers pay to these insurers in premiums each year, have established their own affiliated or
16 “captive” reinsurers. These captive reinsurers provide reinsurance primarily or exclusively for loans
17 the lender originates that require the borrower to pay for private mortgage insurance.

18 48. Under “captive reinsurance arrangements,” the lender refers its borrowers to a private
19 mortgage insurer who agrees to reinsure with the lender’s captive reinsurer. These arrangements
20 require the private mortgage insurer to cede a percentage of the borrowers’ premiums to the lender’s
21 captive reinsurer.

22 49. Captive mortgage reinsurance arrangements raise obvious RESPA kickback problems.
23 Private mortgage insurers are dependent on the lender to obtain business, while the lender is
24 collaborating with the insurer to obtain a share of the borrower’s premium revenue through its captive
25 reinsurer. The insurer stimulates its business by providing a lucrative stream of revenue for the lender
26 via the lender’s captive reinsurer.

27 50. Simply put, as opposed to receiving direct payments for referring its customers to a
28 certain private mortgage insurer, an unscrupulous lender can use a captive reinsurance arrangement to

1 funnel such unlawful kickbacks through its subsidiary reinsurance company.

2 51. Concerned that these transactions would be designed to disguise a funneling of referral
3 fees back to the lender who arranged for the private mortgage insurer to obtain the business, HUD
4 issued a letter dated August 6, 1997 (“HUD letter”) addressing the problem of captive reinsurers and
5 RESPA’s anti-kickback violations. *See* HUD letter attached as Exhibit A.

6 52. The HUD letter concluded that captive reinsurance arrangements were permissible
7 under RESPA only “if the payments to the affiliated reinsurer: (1) are for reinsurance services
8 ‘actually furnished or for services performed’ and (2) are bona fide compensation that does not exceed
9 the value of such services” (emphasis in original).

10 53. The HUD letter focuses the RESPA anti-kickback analysis on whether the arrangement
11 between the lender’s captive reinsurer and the private mortgage insurer represents “a real transfer of
12 risk.” HUD warned that “The reinsurance transaction cannot be a sham under which premium
13 payments . . . are given to the reinsurer even though there is no reasonable expectation that the
14 reinsurer will ever have to pay claims.”

15 54. The HUD letter states “This requirement for a real transfer of risk would clearly be
16 satisfied by a quota share arrangement, under which the reinsurer is bound to participate pro rata in
17 every claim” (emphasis in original).

18 55. The HUD letter contrasts the excess loss method of reinsurance. HUD states that
19 excess loss reinsurance contracts can escape characterization as a referral fee or fee-split only:

20
21 . . .if the band of the reinsurer’s potential exposure is such that a
22 reasonable business justification would motivate a decision to reinsure
23 that band. Unless there is a real transfer of risk, no real reinsurance
services are actually being provided. In either case, the premiums
paid . . . must be commensurate with the risk.

24 56. Notably, state insurance commissioners and federal regulators have investigated and
25 uniformly condemned similar captive reinsurance arrangements in the title insurance industry as sham
26 transactions designed to funnel unlawful kickbacks for business referrals. As a result, a number of
27 offenders paid fines, reimbursed customers and abandoned such arrangements altogether. *See, e.g.,*
28

1 http://www.fntg.com/captive_reinsurance.asp. See also Lori Lesko, *Stewart Faces Renewed Charges*
 2 *of RESPA Reinsurance Violations*, \$42 Million Fine, RESPANews.com, available at:
 3 <http://RESPANews.com>, Archived News Headlines (last accessed June 2, 2008) (noting the California
 4 Department of Insurance's accusation that Stewart Title reported anticipated recoveries from the
 5 captive reinsurers on reported claims from 1998-2006 of zero dollars, thereby indicating no real
 6 transfer of risk or expectation of transfer of risk"); *Insurance Commissioner of the State of California*
 7 *v. Stewart Title Guaranty Co.*, File No. DISP05048942 (Insurance Commissioner of the State of
 8 California June 27, 2007); Janis Mara, *Wells Fargo, Citibank Under Investigation in Alleged Kickback*
 9 *Schemes*, *Inman News*, available at: <http://alta.org/indynews/news.cfm?newsID=2571> (last accessed
 10 June 2, 2008); Steve Zurrier, *Kickbacks Probed*, AllBusiness.com, available at:
 11 <http://www.allbusiness.com/personal-finance/real-estate/941921-1.html> (last accessed June 2, 2008)
 12 (noting, "The problem is that these particular reinsurance companies have yet to pay out any claims,
 13 which is why state insurance officials allege the money sent to the reinsurance companies is a flat-out
 14 kickback"); HUD Reaches RESPA Settlements With Major Lender And Builders For \$1.6 Million,
 15 Press Release dated July 18, 2006, available at: [http://www.hud.gov/news/release.cfm?content=pr06-](http://www.hud.gov/news/release.cfm?content=pr06-086.cfm)
 16 [086.cfm](http://www.hud.gov/news/release.cfm?content=pr06-086.cfm).

17 57. The National Association of Insurance Commissioners ("NAIC") also addressed the
 18 accounting treatment of premiums ceded to captive mortgage reinsurers. Under the annual statement
 19 requirements of the NAIC, private mortgage insurers should not treat as authorized reinsurance
 20 amounts ceded to lender-captive reinsurers where adequate risk is not transferred. Rather, such
 21 amounts should be accounted for under the less beneficial deposit accounting guidelines and identified
 22 as though unauthorized accounting was being utilized.

23 58. Finally, HUD also stated that consumers should be provided with adequate disclosure
 24 concerning their lenders' captive reinsurance arrangements, finding that "consumers would be well
 25 served by a meaningful disclosure and a meaningful choice for consumers having their loans included
 26 in a captive reinsurance program." HUD defined a "meaningful disclosure" as one that "would reveal
 27 that the captive reinsurance arrangement exists, that the lender stands to gain financially under the
 28

1 arrangement, and that the consumer may choose not to have his or her insurance provided by an
2 insurer in such an arrangement. HUD defined a “meaningful choice” as one that “would provide the
3 consumer an easy, non-burdensome opportunity to opt out by, for example, indicating a preference one
4 way or the other on a form.”

5 59. Upon information and belief, PHH did not provide adequate disclosure to its borrowers.
6 Upon information and belief, the Company purposefully provided neither a meaningful disclosure nor
7 a meaningful choice to its borrowers regarding its captive reinsurance arrangements. PHH’s
8 borrowers were not put on notice of their claims and, despite exercising reasonable due diligence,
9 reviewing their loan documents, reasonably could not have discovered their claims within the
10 applicable statute of limitations.

11 **PHH’s Captive Reinsurance Arrangements**

12 60. In connection with the billions of dollars in home loans originated by PHH, many of its
13 borrowers pay for private mortgage insurance.

14 61. PHH enters into “captive reinsurance arrangements,” whereby it refers its borrowers to
15 private mortgage insurers, who agree to reinsure with Atrium. These insurers include at least: AIG
16 United Guaranty, Genworth Mortgage Insurance Corporation, Radian Guaranty Inc., and CMG
17 Mortgage Insurance.

18 62. PHH has a strong financial interest in steering business to private mortgage insurers
19 who, in turn, agree to reinsure with Atrium on terms that will produce significant kickbacks to PHH.

20 63. Atrium enters into reinsurance agreements solely with respect to loans originated by
21 PHH.

22 64. Under PHH’s captive reinsurance arrangements, the primary insurer pays Atrium a
23 percentage of the premiums paid by borrowers on a particular pool of loans; in return, Atrium
24 purportedly agrees to assume a portion of the insurer’s risk with respect to the loans involved.

25 65. In fact, no actual, little or incommensurate risk is actually transferred from the primary
26 insurer to Atrium in exchange for the significant reinsurance payments to Atrium. The actual risk, if
27 any, transferred to Atrium is not commensurate with the premiums it extracts from the private
28

mortgage insurer.

66. The numbers speak for themselves. For instance, during the time frame beginning in 2000 and extending through 2007, PHH's captive reinsurer has collected from private mortgage insurers over \$327,000,000 as its "share" of borrower's private mortgage insurance premiums. In contrast, its "share" of paid insured losses was zero:

YEAR	PREMIUMS RECEIVED BY REINSURER	LOSSES PAID BY REINSURER
2007	\$32,559,000	\$0
2006	\$35,740,000	\$0
2005	\$45,718,000	\$0
2004	\$41,868,000	\$0
2003	\$46,198,000	\$0
2002	\$49,785,000	\$0
2001	\$42,943,000	\$0
2000	\$32,749,000	\$0
TOTAL:	\$327,560,000	\$0

67. As HUD noted during its recent testimony by Assistant Secretary for Regulatory Affairs and Manufactured Housing Gary M. Cunningham before the United States Congress (referring to analogous captive reinsurance arrangements in the title insurance industry):

[W]hen there is a history of little or no claims being paid, or the premium payments to the captive reinsurer far exceed the risk borne by the reinsurer, there is strong evidence that there is an arrangement constructed for the purpose of payment of referral fees or other things of value in violation of Section 8 of RESPA.

68. The millions of dollars collected by PHH through its captive reinsurer have clearly not been commensurate to its actual risk exposure. The Company has received millions of dollars in

1 payments, while bearing little or no risk of loss.

2 69. In reality, PHH's captive reinsurance arrangements were and are sham transactions for
3 collecting illegal kickbacks in return for referring private mortgage insurance business to certain
4 insurers.

5 70. The money PHH collected through its captive reinsurer far exceeded the value of the
6 services, if any, it performed. There was no real transfer of risk or, at least, not a commensurate
7 transfer of risk. The amounts paid were simply disguised kickbacks to PHH for the referral of
8 borrowers to private mortgage insurers.

9 71. These arrangements keep premiums for private mortgage insurance artificially inflated
10 because a percentage of borrowers' premiums are not actually being paid to cover actual risk, but are
11 simply funding illegal kickbacks to lenders. In other words, because the money collected by a lender
12 through its captive reinsurer comes from borrowers' mortgage insurance premiums, borrowers are
13 essentially required to pay for both actual private mortgage insurance coverage and private mortgage
14 insurers' unlawful kickbacks to lenders.

15 72. Amounts paid to lenders as unlawful kickbacks have become a part of the cost of doing
16 business for private mortgage insurers. As a result, private mortgage insurance premiums incorporate
17 the payment of such kickbacks—to the detriment of consumers.

18 **CLASS ACTION ALLEGATIONS**

19 73. Plaintiffs bring this action pursuant to Federal Rules of Civil Procedure 23(a) and
20 23(b)(1), (b)(2) and/or (b)(3) on behalf of a general class consisting of all persons who obtained
21 residential mortgage loans originated and/or acquired by PHH and/or its affiliates and, in connection
22 therewith, purchased private mortgage insurance and whose loans were included within PHH's captive
23 mortgage reinsurance arrangements (the "Class").

24 74. The Class excludes Defendants and any entity in which Defendants have a controlling
25 interest, and their officers, directors, legal representatives, successors and assigns.

26 75. The Class is so numerous that joinder of all members is impracticable.

27 76. A class action is superior to all other available methods for the fair and efficient
28

1 adjudication of this controversy.

2 77. Plaintiffs' claims are typical of the claims of the Class.

3 78. There are questions of law and fact common to the Class, including but not limited to:

4 (a) Whether Defendants' captive reinsurance arrangements involved sufficient
5 transfer of risk;

6 (b) Whether payments to PHH's captive reinsurer were bona fide compensation and
7 solely for services actually performed;

8 (c) Whether payments to PHH's captive reinsurer exceeded the value of any
9 services actually performed;

10 (d) Whether PHH's captive reinsurance arrangements constituted unlawful
11 kickbacks from private mortgage insurers;

12 (e) Whether PHH accepted a portion, split or percentage of borrowers' private
13 mortgage insurance premiums other than for services actually performed; and

14 (f) Whether Defendants are liable to Plaintiffs and the Class for statutory damages
15 pursuant to RESPA § 2607(d)(2).

16 79. These and other questions of law and/or fact are common to the Class and predominate
17 over any questions affecting only individual Class members. Indeed, this is the quintessential case for
18 class action treatment. Defendants' captive reinsurance agreements were not entered into for each
19 individual borrower, but, rather, for pools of loans.

20 80. The same common issues predominate with respect to all members of the Class,
21 regardless of whether their loans were originated by PHH or acquired from third-party lenders.
22 Plaintiffs' sole claim is for violation of Section 8 of RESPA, 12 U.S.C. § 2607. Section 8(b) of
23 RESPA, 12 U.S.C. § 2607(b), does not require a referral, but, as described herein, contains a general
24 prohibition against the acceptance of any unearned settlement services charges. Therefore, regardless
25 of whether PHH or a third-party lender made the initial referral to the private mortgage insurer,
26 Defendants' acceptance of any unearned portion of the private mortgage insurance premiums paid by
27 such borrowers violates RESPA, as described herein.
28

81. Plaintiffs will fairly and adequately represent and protect the interests of the members of the Class. Plaintiffs have no claims antagonistic to those of the Class. Plaintiffs have retained counsel competent and experienced in complex nationwide class action litigation. Plaintiffs' counsel will fairly, adequately and vigorously protect the interests of the Class.

82. Class action status is warranted under Rule 23(b)(1)(A) because the prosecution of separate actions by or against individual members of the class would create a risk of inconsistent or varying adjudications with respect to individual members of the class, which would establish incompatible standards of conduct for Defendants.

83. Class action status is also warranted under Rule 23(b)(1)(B) because the prosecution of separate actions by or against individual members of the class would create a risk of adjudications with respect to individual members of the class which would, as a practical matter, be dispositive of the interests of the other members not parties to the adjudications or substantially impair or impede their ability to protect their interests.

84. Class action status is also warranted under Rule 23(b)(2) because Defendants have acted or refused to act on grounds generally applicable to the class, thereby making appropriate final injunctive relief or corresponding declaratory relief with respect to the class as a whole.

85. Class action status is also warranted under Rule 23(b)(3) because questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and a class action is superior to other available methods for the fair and efficient adjudication of this controversy.

CLAIM FOR RELIEF

Violation of RESPA Section 8, 12 U.S.C. § 2607

86. Plaintiffs hereby incorporate by reference the preceding paragraphs as if they were fully set forth herein.

87. Throughout the Class Period, PHH provided “settlement services” in respect of “federally-related mortgage loans,” as such terms are defined by RESPA §§ 2602(1) and (3).

88. The amounts received by PHH through its captive reinsurance arrangements constituted

1 “things of value” within the meaning of RESPA § 2602(2).

2 89. Plaintiffs and the Class obtained federally-related residential mortgage loans through
3 PHH and paid millions of dollars for private mortgage insurance premiums in connection with their
4 real estate closings. Defendants arranged for an unlawfully excessive split of borrowers’ premiums to
5 be paid to Atrium.

6 90. The millions of dollars in premiums accepted from private mortgage insurers: (a) were
7 not for services actually furnished or performed; and/or (b) exceeded the value of such services.

8 91. The millions of dollars accepted by PHH through its captive reinsurance arrangements
9 constituted fees, kickbacks or things of value pursuant to agreements with private mortgage insurers
10 that business incident to real estate settlement services involving federally-related mortgage loans
11 would be referred to such insurers. Such practice violated RESPA, 12 U.S.C. 2607(a). Atrium—
12 PHH’s subsidiary—participated in the scheme and served as the direct conduit by which the kickbacks
13 were funneled. Atrium agreed to provide purported “reinsurance” services involving mortgage
14 insurance paid by Plaintiffs and the Class.

15 92. In connection with transactions involving federally-related mortgage loans, PHH
16 accepted a portion, split or percentage of charges received by private mortgage insurers for the
17 rendering of real estate settlement services other than for services actually performed, in violation of
18 RESPA, 12 U.S.C. 2607(b). The money paid by private mortgage insurers to PHH and accepted by
19 PHH through its captive reinsurer was a portion, split or percentage of the private mortgage insurance
20 premiums paid by PHH’s customers. Atrium—PHH’s subsidiary—participated in the scheme and
21 served as the direct party to which the split was paid. Atrium agreed to provide purported
22 “reinsurance” services involving mortgage insurance paid by Plaintiffs and the Class.

23 93. Plaintiffs and the Class were harmed by Defendants’ unlawful kickback scheme.

24 94. First, Plaintiffs and the Class were overcharged for mortgage insurance. Kickbacks and
25 unearned fees unnecessarily and artificially inflate settlement service charges. Under PHH’s scheme,
26 the mortgage insurance premiums paid by Plaintiffs and the Class necessarily and wrongly included
27 payments for both: (a) actual mortgage insurance services; and (b) payments unlawfully kicked back to
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1 PHH's captive reinsurer that far exceeded the value of any services performed and, were, in fact,
2 illegal referral fees.

3 95. Second, *regardless* of whether Plaintiffs and the Class were overcharged for private
4 mortgage insurance, and *regardless* of the reasonableness or unreasonableness of the rates Plaintiffs
5 paid for private mortgage insurance, under RESPA, Plaintiffs and the Class were, as a matter of law,
6 entitled to purchase settlement services from providers that did not participate in unlawful kickback
7 and/or fee-splitting schemes. Congress has expressly provided for private enforcement of this
8 protected right by empowering consumers to recover statutory damages from offending parties. *See*
9 *Edwards v. The First American Corp., et. al.*, 517 F. Supp. 2d 1199, 1204 (C.D. Cal. 2007).

10 96. Plaintiffs allege that Defendants accepted unlawful kickback payments and/or an
11 unearned portion of settlement service charges in violation of RESPA—allegations and claims
12 completely distinct and separate from whether the price he paid for settlement services was “unfair.”

13 97. Defendants therefore violated RESPA, 12 U.S.C. § 2607. Accordingly, pursuant to the
14 clear and unambiguous language of 12 U.S.C. § 2607(d), Plaintiffs and the Class are entitled to
15 recover from Defendants an amount equal to three times the amounts they have paid or will have paid
16 for private mortgage insurance as of the date of judgment. *See Edwards*, 517 F. Supp. 2d at 1203-
17 1204.

18 98. In accordance with RESPA, 12 U.S.C. § 2607(d), Plaintiffs also seek attorneys' fees
19 and costs of suit.

20 **EQUITABLE TOLLING/FRAUDULENT CONCEALMENT**

21 99. Applicable statutes of limitation may be tolled based upon principles of equitable
22 tolling, fraudulent concealment and/or the discovery rule. With respect to the putative Class members
23 whose claims would otherwise be barred by the applicable statute of limitations, equitable tolling is
24 available under RESPA and should apply. Such putative Class members could not, despite the
25 exercise of due diligence, have discovered the underlying basis for their claims. Further, Defendants
26 knowingly and actively concealed the basis for Plaintiffs' claims by engaging in a scheme that was, by
27 its very nature and purposeful design, self-concealing. For these reasons, any delay by the members of
28

1 the putative Class was excusable.

2 100. Due to the complex, undisclosed and self-concealing nature of PHH's scheme to collect
3 illegal kickbacks from private mortgage insurers, the putative Class members whose claims accrued
4 prior to one year preceding the filing of this Complaint did not possess sufficient information or
5 possess the requisite expertise in order to enable them to discover the true nature of Defendants'
6 captive reinsurance arrangements.

7 101. As above-noted, HUD has clearly stated that consumers should be provided with
8 adequate disclosure concerning their lenders' captive reinsurance arrangements, finding that
9 "consumers would be well served by a meaningful disclosure and a meaningful choice for consumers
10 having their loans included in a captive reinsurance program." HUD defined a "meaningful
11 disclosure" as one that "would reveal that the captive reinsurance arrangement exists, that the lender
12 stands to gain financially under the arrangement, and that the consumer may choose not to have his or
13 her insurance provided by an insurer in such an arrangement." HUD defined a "meaningful choice" as
14 one that "would provide the consumer an easy, non-burdensome opportunity to opt out by, for
15 example, indicating a preference one way or the other on a form."

16 102. Upon information and belief, PHH did not provide adequate disclosure to its borrowers.
17 Upon information and belief, the Company purposefully provided neither a meaningful disclosure nor
18 a meaningful choice to its borrowers regarding its captive reinsurance arrangements. PHH's
19 borrowers were not put on notice of their claims and, despite exercising reasonable due diligence,
20 reviewing their loan documents, reasonably could not have discovered their claims within the
21 applicable statute of limitations.

22 103. This complex action is dissimilar to a simple type of RESPA case where, for example,
23 an attentive borrower may easily determine—from a careful examination of her HUD-1 settlement
24 statement—that too much money is being paid from her proceeds to her lender, real estate agent, title
25 insurer or other settlement service provider. Rather, the conduct described herein occurs behind closed
26 doors, with a wispy trail virtually impossible for the homeowner to follow.

27 104. In addition to the self-concealing nature of the reinsurance scheme and Defendants' acts
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1 in furtherance of the concealment described above, the captive reinsurance framework also made the
2 fraudulent conduct substantially difficult, if not impossible, for the challenged Class members to
3 discover. For example, Atrium is a closely-held insurance company that does not sell to the general
4 public and, consequently, is subject to far less regulatory oversight than commercial insurance
5 companies that sell to the general public.

6 105. Indeed, the named Plaintiffs in this action were able to discover the underlying basis for
7 the claims alleged herein only with the assistance and investigation of counsel. Plaintiffs and the
8 putative Class members simply had no basis upon which to investigate the validity of the shrouded
9 payments to Atrium for purported reinsurance. Putative Class members' delay was excusable because
10 they did not discover, and reasonably could not have discovered, Defendants' conduct as alleged
11 herein absent specialized knowledge and/or assistance of counsel.

12 106. Further, PHH fraudulently concealed the facts and circumstances giving rise to the
13 claims asserted herein. PHH made affirmative, intentional misrepresentations concerning its captive
14 reinsurance program. PHH affirmatively represented to Plaintiffs and the Class that any amounts it
15 received from its captive reinsurance arrangements were for services actually performed. For
16 example, in the 2007 10-K, PHH represented that its captive reinsurer provided actual reinsurance
17 services in return for the premiums that it received from its borrowers private mortgage insurance
18 providers. *See 2007 10-K*. In reality, as PHH undoubtedly knew, its reinsurer provided no real
19 services and, rather, was merely a conduit for unlawful kickbacks and revenue-sharing from private
20 mortgage insurers. PHH concealed information that could have put the putative Class members on
21 notice that there was inadequate assumption of risk by Atrium and that, accordingly, the Company was
22 merely accepting hundreds of millions of dollars of borrowers' insurance premiums as an unlawful
23 kickback.

24 107. Further, by purposefully arranging for kickbacks to be funneled through Atrium—
25 rather than paid directly to PHH Home Loans or PHH Mortgage, Defendants affirmatively acted to
26 conceal and prevent Plaintiffs from discovering the underlying basis for this action.

27 108. Further, pursuant to RESPA § 2604(c) and the accompanying regulations set forth in 24
28

1 C.F.R. 3500.7, if PHH required the use of a particular provider of settlement service, it was obligated
2 to describe the nature of any relationship between PHH and such provider. PHH required the use of
3 the private mortgage insurers to whom it referred Plaintiffs and the Class, yet failed to adequately
4 describe its relationship with such settlement service providers.

5 109. Accordingly, the putative Class members did not possess sufficient information to put
6 them on notice: (a) of the true nature of PHH's captive reinsurance arrangements; (b) that anything
7 improper or actionable may have occurred with respect to such arrangements; and/or (c) that their
8 rights under RESPA were being violated. The average homebuyer is not an insurance expert and is
9 not an actuary. PHH intentionally interfered with Plaintiffs' and the absent Class members' discovery
10 of their claims by making false and/or misleading statements in its SEC filings and by purposefully
11 refusing to provide the meaningful disclosure and meaningful choice articulated by HUD. Thus, the
12 putative class members were not put on notice of PHH's wrongdoing.

13 110. The putative class members exercised due diligence by fully participating in their loan
14 transactions and reviewing relevant loan documents. *See, e.g., Boudin v. Residential Essentials, LLC*,
15 No. 07-0018, 2007 WL 2023466, at * 5 (S.D. Ala. 2007). Because of Defendants' actions and because
16 of the nature of the reinsurance scheme, the absent putative Class members were not put on notice of
17 Defendants' wrongdoing despite exercising due diligence.

18 111. Any delay by the absent putative Class members is excusable; further, Defendants'
19 should be estopped from relying upon the applicable statute of limitations. Accordingly, Plaintiffs and
20 the Class contend that it would be inequitable for the Court to apply the one-year limitation period set
21 forth in RESPA § 16, 12 U.S.C. § 2614 in a way that would preclude the claim of any Class member.
22 Such a harsh application would unfairly punish the very consumers RESPA was designed to protect,
23 while rewarding unscrupulous violators.

24 **PRAYER FOR RELIEF**

25 WHEREFORE, Plaintiffs request that this Court enter a judgment against Defendants and in
26 favor of Plaintiffs and the Class and award the following relief:
27
28

1 A. This action be certified as a class action pursuant to Rule 23 of the Federal Rules of
2 Civil Procedure, declaring Plaintiffs as representatives of the Class and Plaintiffs' counsel as counsel
3 for the Class;

4 B. The conduct alleged herein be declared, adjudged and decreed to be unlawful;

5 C. Plaintiffs and the Class be awarded statutory damages pursuant to RESPA § 8(d)(2), 12
6 U.S.C. § 2607(d)(2);

7 D. An order granting Plaintiffs and the Class costs of suit, including reasonable attorneys'
8 fees and expenses; and

9 E. An order granting Plaintiffs and the Class such other, further and different relief as the
10 nature of the case may require or as may be determined to be just, equitable and proper by this Court.

11 **DEMAND FOR JURY TRIAL**

12 Plaintiffs hereby demand a trial by jury as to all claims in this action.

13
14 Dated: December 10, 2010

Respectfully submitted,

15 **BARROWAY TOPAZ KESSLER**
16 **MELTZER & CHECK, LLP**

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CERTIFICATION

I hereby certify that, on December 10, 2010, a copy of the foregoing document was filed electronically. Notice of this filing will be sent by e-mail to all parties by operation of the court's electronic filing system or by mail to anyone unable to accept electronic filing as indicated on the Notice of Electronic Filing. Parties may access this filing through the Court's EM/ECF system.

Dated: December 10, 2010

/s/ Edward W. Ciolko
Edward W. Ciolko

ClassAction.org

This complaint is part of ClassAction.org's searchable class action lawsuit database and can be found in this post: [PHH Settlement Offers \\$875 Payouts to Resolve Class Action Over Alleged Mortgage Insurance Kickbacks](#)
